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January 27, 1982

SUMMARY AND OUTLOOK

Prepared for the Federal Open Market Committee

By the staff of the Board of Governors of the Federal Reserve System

DOMESTIC NONFINANCIAL DEVELOPMENTS

Summary. Economic activity contracted sharply during the fourth quarter, although the rate of decline in some sectors appears to have moderated around the turn of the year. Retail sales leveled off in November and December in real terms, and domestic auto sales in early January were moderately above their fourth quarter rate. Housing starts, although still very depressed, were a bit higher in December than in the preceding several months. But real business fixed investment fell sharply over the quarter. And, with inventories still high relative to sales, cutbacks in industrial production appear to have continued into January. Recent data show a widespread moderation of wage and price increases.

Retail sales rose slightly in December, but sales in the GAF grouping of stores were up more than 1 percent in nominal terms following a decline over the preceding three months. Domestic auto sales fell further in December, to just under 5 million units at an annual rate, but moved up a bit in the first 20 days of January.

The housing market appeared to improve somewhat in December, with both housing starts and sales of existing homes rising slightly. However, those increases may be temporary; mortgage rates have risen since then and particularly bad weather conditions in January may have retarded activity.

Business spending for capital goods declined in December. And, indicators of near-term business investment suggest that the contraction in this sector will continue into 1982. Orders for nondefense capital goods and contracts for business construction were particularly weak in

the second half of last year. The Commerce Department survey of spending plans, which generally has been too optimistic during a recession, projects capital expenditures about unchanged in real terms for 1982.

Through November, the ratio of inventories to sales was still rising, although the rate of stockbuilding had begun to slow, particularly in the manufacturing and retail trade sectors. But with sales still weak, there were widespread production cutbacks again in December. The index of industrial production dropped 2.1 percent, following a 1.9 percent decline in November. Preliminary data for January show that auto assembly schedules were cut sharply further--to an annual rate of 3.6 million units--and that steel output was again reduced.

With production dropping, demand for labor has continued to weaken. Payroll employment declined 300,000 in December, and the rise in layoffs pushed the unemployment rate up another 1/2 percentage point to 8.9 percent. The effects of persistent slack in the labor market appear to have held down the rate of wage increase for production workers during 1981. The index of average hourly earnings rose at a 7.1 percent annual rate in the fourth quarter, bringing the rise for the year to 8.3 percent--down from 9.6 percent during 1980. The number of wage concessions spread last year, and recently a new Teamsters contract has been proposed that would significantly limit labor cost increases in unionized trucking. Negotiations, which may result in similar adjustments, have begun in the auto industry.

Measures of inflation indicate a broad slowing of price increases in recent months. The consumer price index rose at a 5-1/4 percent annual rate over the final quarter of last year, with moderation evident for

most major components of the index. Over the year as a whole, the CPI rose less than 9 percent--the first single-digit rate since 1978. At the producer level, rates of price increase for a wide range of industrial materials and construction supplies slowed substantially over the second half of 1981, and advances in capital equipment prices moderated from the double-digit rates that persisted through early 1981.

Outlook. The staff now expects that real GNP will decline at a 4 percent annual rate in the current quarter, following a drop at a 5-1/4 percent rate in the final quarter of 1981. Much of the continued decline is expected to result from a further contraction in business fixed investment and a liquidation of inventories. Household spending is expected to partially reverse its fourth quarter contraction. Auto sales are anticipated to pick up a bit, owing in part to new purchase incentive programs, and housing starts are projected to average slightly above their fourth quarter level. To the extent that activity early in the quarter is held down by adverse weather, the staff assumes that these cutbacks are largely made up by the end of the quarter. Nevertheless, the inventory correction now under way is expected to result in further declines in industrial production, and the unemployment rate is projected to continue to increase, reaching 9-1/2 percent early this year.

The staff projections in this Greenbook have been extended through 1983. The projection is based on the assumption that growth of M-1 will slow from around 4 percent over the four quarters of this year to 3-1/2 percent during 1983. Given these targets, short-term interest rates are expected to fluctuate near their recent higher levels throughout the projection period, while long-term rates may tend downward as inflation continues to abate.

On the fiscal side, given current tax and spending policies and the staff's economic assumptions, the budget deficit in FY 1982 is projected to total \$107 billion. The principal fiscal policy influence in FY 1983 is the scheduled 10 percent cut in personal income tax rates effective July 1, 1983, which is anticipated to lower annual receipts by \$32 billion. In addition, the staff has assumed new fiscal restraint measures on both the spending and revenue sides. Outlays in FY 1983 are assumed to be reduced about \$15 billion below the amount needed to maintain nondefense programs at their FY 1982 level of services, and federal receipts are assumed to be boosted by a package of revenue measures worth about \$5 billion. On balance, these measures are anticipated to result in a budget deficit of around \$140 billion in FY 1983.

Given these underlying policy assumptions, the recovery in real activity later this year is projected to be comparatively weak, despite the substantial tax cut on July 1. Following the first-quarter decline, real GNP is projected to increase at a 3-1/4 percent annual rate over the remainder of 1982, and then to rise by about 2-1/4 percent next year. The unemployment rate is projected to drift down a bit later this year and during 1983, but to remain close to 9 percent throughout most of the period.

The stringent financial conditions and the underutilization of capacity persisting into 1983 are the principal restraint on investment spending. The current retrenchment in business capital spending is expected to continue throughout most of 1982, and firms are anticipated to increase their spending only very slowly during 1983. Business firms are also expected to keep a tight rein on inventory accumulation.

Residential construction activity is projected to rise moderately over the course of the projection, although housing starts are expected to reach only 1-1/4 million units a year at the end of 1983.

The reduction in income taxes is a major influence boosting consumer outlays, particularly in the second half of this year and next. Demand for domestic autos is anticipated to improve over the remainder of this year from the recent very depressed level. Nevertheless, at 6-3/4 million units, sales remain well below the 8-1/4 million unit annual average of the late 1970s. Sluggish homebuilding is expected to limit demand for other household durable goods.

The external sector is expected to continue to be a source of weakness throughout the projection period. Sluggish growth abroad and the appreciation of the dollar in 1981 are both expected to hold down exports. With the volume of imports rising slowly after mid-1982, net exports are projected to continue to decline until late 1983.

The recent improvement in inflation is projected to be sustained in early 1982, as economic activity turns around, despite some temporary near-term upward pressure on consumer prices from reduced food supplies. Subsequently, with growth in demand moderate, inflation is expected to continue to unwind gradually over the course of the next two years. Productivity trends are anticipated to improve only slowly; the increase in output per hour is projected to average 1-1/2 percent a year through 1983--somewhat above its longer run trend. Wage increases are expected to be limited by the slack in the labor market, and the trend toward lowering labor costs in industries facing financial problems is

anticipated to continue. The gross domestic business product fixed-weighted price index is projected to rise at a 6-3/4 percent rate during 1982 and at a 5-1/4 percent rate during 1983.

Detailed data for these projections are shown in the tables that follow.

STAFF GNP PROJECTIONS

Percent changes, annual rate										
		Gross domestic business product fixed-weighted price index						Unemployment rate (percent)		
Nominal GNP		Real GNP		Total		Excluding food and energy				
12/16/81	1/27/82	12/16/81	1/27/82	12/16/81	1/27/82	12/16/81	1/27/82	12/16/81	1/28/82	
Annual changes:										
1980 <u>1/</u>	8.8	8.8	-.2	-.2	9.8	9.8	8.2	8.2	7.1	7.1
1981 <u>1/</u>	11.1	11.3	1.8	1.9	9.4	9.4	9.4	9.0	7.6	7.6
1982	6.9	6.3	-.6	-.9	7.6	7.4	7.7	7.6	8.7	9.4
1983	--	8.3	--	2.6	--	5.7	--	5.4	--	9.2
Quarterly changes:										
1981-Q1 <u>1/</u>	19.2	19.2	8.6	8.6	10.5	10.5	8.4	8.4	7.4	7.4
1981-Q2 <u>1/</u>	4.7	4.7	-1.6	-1.6	8.2	8.2	9.7	9.7	7.4	7.4
1981-Q3 <u>1/</u>	10.2	11.4	.6	1.4	9.8	9.9	14.4	11.5	7.2	7.2
1981-Q4 <u>1/</u>	3.0	2.7	-5.5	-5.2	7.7	7.1	5.5	7.7	8.4	8.4
1982-Q1	4.6	2.5	-2.2	-4.0	7.1	6.9	7.0	6.4	8.9	9.3
1982-Q2	9.0	8.2	1.9	1.3	7.4	7.3	7.0	7.0	9.2	9.5
1982-Q3	10.8	10.9	4.1	4.5	7.1	6.8	6.6	6.5	9.1	9.4
1982-Q4	10.0	10.0	3.1	3.7	6.4	5.9	6.4	5.9	9.0	9.3
1983-Q1	--	7.0	--	1.4	--	5.5	--	5.1	--	9.3
1983-Q2	--	6.5	--	1.4	--	5.3	--	4.8	--	9.3
1983-Q3	--	8.7	--	3.9	--	5.1	--	4.5	--	9.2
1983-Q4	--	8.1	--	2.7	--	5.0	--	4.7	--	9.1
Two-quarter changes:										
1981-Q2 <u>1/</u>	11.7	11.7	3.4	3.4	9.2	9.2	9.0	9.0	-.1	-.1
1981-Q4 <u>1/</u>	6.5	7.0	-2.5	-2.0	8.7	8.5	9.9	9.6	1.0	1.0
1982-Q2	6.8	5.3	-.2	-1.4	7.2	7.1	7.0	6.7	.8	1.1
1982-Q4	10.4	10.5	3.6	4.1	6.7	6.3	6.5	6.2	-.2	-.2
1983-Q2	--	6.7	--	1.4	--	5.4	--	4.9	--	.0
1983-Q4	--	8.4	--	3.3	--	5.1	--	4.6	--	-.2
Four-quarter changes:										
1980-Q4 <u>1/</u>	9.4	9.4	-.3	-.3	9.7	9.7	8.6	8.6	1.6	1.6
1981-Q4 <u>1/</u>	9.1	9.3	.4	.7	9.0	8.9	9.5	9.3	.9	.9
1982-Q4	8.6	7.9	1.7	1.3	7.0	6.7	6.7	7.5	.6	.9
1983-Q4	--	7.6	--	2.3	--	5.2	--	5.3	--	-.2

1/ Actual.2/ Percent change from two quarters earlier.3/ Percent change from four quarters earlier.

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GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Quarterly figures are seasonally adjusted. Expenditures and income
figures are billions of current dollars at annual rates.)

	1980				1981			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Gross national product	2571.7	2564.8	2637.3	2730.6	2853.0	2885.8	2965.0	2984.9
Final purchases	2569.1	2557.4	2653.4	2748.0	2848.5	2862.5	2937.6	2967.3
Private	2052.3	2027.4	2119.9	2189.4	2272.0	2285.1	2348.7	2351.6
Excluding net exports	2044.1	2010.3	2075.4	2166.1	2242.8	2264.3	2319.4	2335.6
Personal consumption expenditures	1631.0	1626.8	1682.2	1751.0	1810.1	1829.1	1883.9	1909.5
Goods	882.0	858.4	883.0	926.8	964.3	962.6	987.5	987.3
Services	749.0	768.4	799.2	824.2	845.8	866.5	896.4	922.2
Gross private domestic investment	415.6	390.9	377.1	397.7	437.1	458.6	463.0	443.6
Residential construction	115.2	93.6	99.2	113.0	116.7	110.7	100.5	93.4
Business fixed investment	297.8	289.8	294.0	302.1	315.9	324.6	335.1	332.6
Change in business inventories	2.5	7.4	-16.0	-17.4	4.5	23.3	27.5	17.6
Nonfarm	1.5	6.1	-12.3	-14.0	6.8	21.5	23.1	12.2
Net exports of goods and services <u>1/</u>	8.2	17.1	44.5	23.3	29.2	20.8	29.3	16.0
Exports	337.3	333.3	342.4	346.1	367.4	368.2	368.0	363.0
Imports	329.1	316.2	297.9	322.7	338.2	347.5	338.7	347.1
Gov't. purchases of goods and services	516.8	530.0	533.5	558.6	576.5	577.4	588.9	615.7
Federal <u>2/</u>	190.0	198.7	194.9	212.0	221.6	219.5	226.4	246.7
State and local	326.8	331.3	338.6	346.6	354.9	357.9	362.5	369.0
Gross national product in constant (1972) dollars	1501.9	1463.3	1471.9	1485.6	1516.4	1510.4	1515.8	1495.6
Personal income	2088.2	2114.5	2182.1	2256.2	2319.8	2368.5	2441.7	2484.4
Wage and salary disbursements	1314.7	1320.4	1341.8	1397.8	1442.9	1467.0	1498.5	1522.9
Disposable personal income	1765.1	1784.1	1840.6	1897.0	1947.8	1985.6	2042.0	2086.4
Saving rate (percent)	4.9	6.2	6.1	5.1	4.6	5.4	5.2	6.0
Corporate profits with I.V.A. and C.C. Adj	200.2	169.3	177.9	183.3	203.0	190.3	195.7	167.0
Corporate profits before tax	277.1	217.9	237.6	249.5	257.0	229.0	234.4	200.7
Federal government surplus or deficit (-) (N.I.A. basis)	-36.3	-66.5	-74.2	-67.9	-46.6	-47.2	-55.7	-96.4
High employment surplus or deficit (-) <u>3/</u>	-17.1	-21.5	-21.1	-13.3	.4	6.6	11.5	-21.1
State and local government surplus or deficit (-) (N.I.A. basis)	26.6	23.9	28.6	37.1	36.9	36.1	37.8	35.5
Excluding social insurance funds	1.3	-1.7	.9	8.1	6.6	4.3	5.1	1.8
Civilian labor force (millions)	104.2	104.7	105.0	105.2	105.8	106.8	106.4	106.8
Unemployment rate (percent)	6.2	7.3	7.5	7.5	7.4	7.4	7.2	8.4
Nonfarm payroll employment (millions)	90.8	90.5	90.2	90.8	91.2	91.5	91.9	91.5
Manufacturing	20.8	20.3	20.0	20.2	20.2	20.4	20.5	20.0
Industrial production (1967=100)	152.6	144.5	142.3	148.7	151.8	152.5	153.0	146.3
Capacity utilization: all mfg. (percent)	83.4	77.9	75.9	79.1	79.9	79.8	79.3	74.8
Materials (percent)	85.8	78.8	75.2	80.1	82.2	81.2	81.2	75.3
Housing starts, private (million units, A.R.)	1.23	1.06	1.39	1.54	1.39	1.18	.97	.90
New auto sales, (millions, A.R.)	10.65	7.68	8.80	9.04	9.96	7.89	9.04	7.37
Domestic models	7.87	5.53	6.51	6.57	7.31	5.63	6.90	5.13
Foreign models	2.77	2.14	2.29	2.47	2.66	2.25	2.14	2.24

- 1/ Balance of payments data and details underlying these estimates are shown in the International Developments section of this part of the Greenbook.
- 2/ Components of purchases and total receipts and total expenditures are shown in the Federal Sector Accounts table which follows.
- 3/ Estimates in table are evaluated at a 5.1 percent high employment unemployment rate. Evaluated at a 6.1 percent unemployment rate, the high employment budget would show a deficit of \$37.8 billion in 1980-Q4 and a deficit of 47.2 billion in 1981-Q4.

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PERCENT CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS
(Annual rates compounded quarterly)

	1980				1981			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) dollars</u>								
Gross national product	3.1	-9.9	2.4	3.8	8.6	-1.6	1.4	-5.2
Final purchases	3.1	-10.4	4.1	4.4	6.9	-4.7	.3	-3.6
Private	2.2	-13.3	6.5	4.9	7.3	-4.5	.8	-6.1
Excluding net exports	-.4	-14.4	4.6	8.5	6.7	-3.1	1.9	-4.2
Personal consumption expenditures	.8	-9.8	5.1	7.0	5.8	-2.1	3.3	-1.8
Goods	-.3	-17.7	4.0	10.2	9.8	-5.3	3.8	-5.3
Services	2.1	.0	6.4	3.7	1.4	1.6	2.6	2.2
Gross private domestic investment	-5.6	-28.9	-10.0	11.1	24.2	16.1	3.3	-23.4
Residential structures	-24.2	-60.2	16.0	64.2	3.6	-23.4	-36.2	-26.9
Business fixed investment	2.2	-19.9	-1.5	4.0	13.3	-2.1	6.9	-10.9
Gov't. purchases of goods and services	6.9	2.5	-5.0	2.2	5.4	-5.6	-1.5	7.1
Federal	18.9	11.9	-13.1	2.0	14.8	-8.4	3.1	19.4
National defense	9.8	6.2	-.1	5.9	1.1	2.6	7.9	7.5
State and local	.6	-2.8	.3	2.3	.2	-3.8	-4.2	.1
Disposable personal income	1.3	-4.9	4.1	2.9	3.0	1.4	2.6	1.3
<u>Current dollars</u>								
Gross national product	12.6	-1.1	11.8	14.9	19.2	4.7	11.4	2.7
Final purchases	12.0	-1.8	15.9	15.0	15.5	2.0	10.9	4.1
Private	10.7	-4.8	19.5	13.8	16.0	2.3	11.6	.5
Excluding net exports	10.6	-6.5	13.6	18.7	14.9	3.9	10.1	2.8
Personal consumption expenditures	12.9	-1.0	14.3	17.4	14.2	4.3	12.5	5.6
Goods	13.1	-10.3	12.0	21.4	17.2	-.7	10.8	-.1
Services	12.7	10.8	17.0	13.1	10.9	10.1	14.6	12.0
Gross private domestic investment	5.6	-21.8	-13.3	23.7	45.9	21.1	3.9	-15.7
Residential structures	-16.7	-56.4	25.7	68.5	14.0	-19.2	-32.1	-25.2
Business fixed investment	11.0	-10.4	6.0	11.5	19.6	11.4	13.6	-3.0
Gov't. purchases of goods and services	17.5	10.6	2.6	20.2	13.5	.6	8.2	19.5
Federal	29.5	19.8	-7.5	40.2	19.3	-3.7	13.1	41.2
National defense	23.2	12.4	8.4	35.0	10.4	8.7	16.9	33.8
State and local	11.2	5.6	9.1	9.7	10.0	3.3	5.3	7.4
Disposable personal income	13.5	4.4	13.3	12.8	11.2	8.0	11.8	9.0
Personal income	11.5	5.1	13.4	14.3	11.8	8.7	12.9	7.2
Wage and salary disbursements	10.5	1.8	6.6	17.8	13.5	6.9	8.9	6.7
Corporate profits with IVA & C.C. Adj.	24.8	-48.9	21.9	12.7	50.4	-22.8	11.8	-47.0
Corporate profits before tax	38.6	-61.8	41.4	21.6	12.6	-37.0	9.8	-46.5
Nonfarm payroll employment	1.5	-1.6	-1.0	2.7	1.8	1.4	1.7	-1.8
Manufacturing	-2.4	-9.7	-5.9	3.7	.5	4.2	2.4	-9.4
Nonfarm business sector								
Output per hour	.3	-2.9	3.6	-.2	4.3	1.4	-1.6	-6.5
Compensation per hour	10.2	11.3	9.0	9.8	11.6	9.6	9.3	7.5
Unit labor costs	9.9	14.6	5.3	10.1	7.0	8.1	11.1	13.6
GNP implicit deflator ^{1/}	9.3	9.8	9.2	10.7	9.8	6.4	9.9	8.4
Gross domestic business product								
fixed-weighted price index ^{2/}								
Excluding food and energy	7.4	9.5	9.3	8.2	8.4	9.7	11.5	7.7
Consumer price index (all urban)	16.5	13.1	7.7	12.9	10.8	7.5	12.0	7.7
Industrial production	.3	-19.6	-6.2	19.2	8.3	1.9	1.3	-16.4

^{1/} Excluding Federal pay increases, rates of change were: 1980-Q1, 9.2 percent; 1980-Q4, 9.7 percent; 1981-Q1, 9.7 percent; 1981-Q4, 7.4 percent.

^{2/} Uses expenditures in 1972 as weights.

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GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Quarterly figures are seasonally adjusted. Expenditures and income
figures are billions of current dollars at annual rates.)

	Projected							
	1982				1983			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Gross national product	3003.1	3063.1	3143.3	3219.3	3274.0	3325.8	3396.2	3463.1
Final purchases	3011.1	3065.1	3139.3	3212.3	3266.5	3317.8	3387.7	3454.1
Private	2392.8	2442.2	2505.7	2562.3	2606.4	2647.4	2706.3	2755.2
Excluding net exports	2377.5	2429.8	2497.5	2556.9	2601.0	2643.5	2701.4	2748.9
Personal consumption expenditures	1950.1	1994.6	2052.1	2099.7	2133.4	2167.0	2215.2	2251.1
Goods	1002.3	1021.8	1054.8	1081.9	1095.1	1108.1	1135.0	1151.9
Services	947.8	972.8	997.3	1017.8	1038.3	1058.9	1080.2	1099.2
Gross private domestic investment	419.4	433.2	449.4	464.2	475.1	484.5	494.7	506.8
Residential construction	93.4	97.9	103.9	109.9	113.9	116.4	119.9	125.4
Business fixed investment	334.0	337.3	341.5	347.3	353.7	360.1	366.3	372.4
Change in business inventories	-8.0	-2.0	4.0	7.0	7.5	8.0	8.5	9.0
Nonfarm	-8.0	-2.0	4.0	7.0	7.5	8.0	8.5	9.0
Net exports of goods and services <u>1/</u>	15.3	12.4	8.2	5.4	5.4	3.9	4.9	6.3
Exports	354.1	352.3	355.8	363.4	371.7	378.8	389.3	399.5
Imports	338.8	339.9	347.7	358.0	366.3	374.9	384.5	393.2
Gov't. purchases of goods and services	618.3	622.9	633.6	650.0	660.1	670.4	681.4	698.9
Federal <u>2/</u>	244.1	243.7	249.3	260.4	266.0	272.1	278.5	291.3
State and local	374.2	379.2	384.3	389.6	394.1	398.3	402.9	407.6
Gross national product in constant (1972) dollars	1480.5	1485.2	1501.6	1515.4	1520.8	1526.1	1540.6	1550.9
Personal income	2519.6	2566.2	2628.7	2679.2	2716.3	2758.0	2813.4	2860.6
Wage and salary disbursements	1535.2	1558.1	1587.5	1624.7	1650.5	1677.3	1708.4	1743.9
Disposable personal income	2118.8	2156.8	2243.7	2285.3	2315.7	2348.8	2425.3	2462.3
Saving rate (percent)	5.4	5.0	6.1	5.6	5.4	5.2	6.2	6.1
Corporate profits with I.V.A. and C.C. Adj.	148.0	159.4	182.4	193.3	192.7	192.9	206.7	213.9
Corporate profits before tax	176.8	185.4	205.0	212.3	206.9	202.0	210.3	211.8
Federal government surplus or deficit (-) (N.I.A. basis)	-103.3	-100.9	-143.6	-139.4	-131.7	-131.0	-167.2	-168.5
High employment surplus or deficit (-) <u>3/</u>	-7.0	7.0	-37.4	-32.5	-20.2	-14.7	-55.4	-54.8
State and local government surplus or deficit (-) (N.I.A. basis)	33.6	35.8	39.6	39.1	40.0	41.3	43.7	45.5
Excluding social insurance funds	-1.4	-.4	2.1	.2	-.1	-.1	1.0	1.4
Civilian labor force (millions)	107.1	107.4	107.6	107.9	108.2	108.5	108.8	109.0
Unemployment rate (percent)	9.3	9.5	9.4	9.3	9.3	9.3	9.2	9.1
Nonfarm payroll employment (millions)	90.8	90.7	90.8	91.2	91.4	91.6	92.0	92.3
Manufacturing	19.3	19.2	19.3	19.6	19.7	19.8	20.0	20.2
Industrial production (1967=100)	141.3	143.0	145.9	147.6	148.7	149.7	151.7	153.5
Capacity utilization: all mfg. (percent)	71.5	71.9	72.9	73.3	73.4	73.3	73.8	74.2
Materials (percent)	70.6	71.6	73.3	73.9	74.0	74.2	75.0	75.6
Housing starts, private (million units, A.R.)	.95	1.05	1.15	1.20	1.20	1.20	1.25	1.25
New auto sales, (millions, A.R.)	8.00	8.50	9.10	9.10	9.20	9.30	9.40	9.5
Domestic models	5.70	6.10	6.60	6.60	6.70	6.80	6.90	7.0
Foreign models	2.30	2.40	2.50	2.50	2.50	2.50	2.50	2.5

1/ Balance of payments data and details underlying these estimates are shown in the International Developments section of this part of the Greenbook.

2/ Components of purchases and total receipts and total expenditures are shown in the Federal Sector Accounts table which follows.

3/ Estimates in table are evaluated at a 5.1 percent high employment unemployment rate. Evaluated at a 6.1 percent unemployment rate, the high employment budget would show a deficit of \$60.2 billion in 1982-Q4, and a deficit of \$83.3 billion in 1983-Q4.

CONFIDENTIAL - FR
CLASS II FOMC

PERCENT CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS
(Annual rates compounded quarterly)

	-----Projected-----							
	1982				1983			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) dollars</u>								
Gross national product	-4.0	1.3	4.5	3.7	1.4	1.4	3.9	2.7
Final purchases	-.7	.4	3.7	3.3	1.4	1.3	3.8	2.6
Private	.2	1.2	4.4	3.9	1.5	1.3	4.3	2.7
Excluding net exports	.3	2.0	5.1	4.3	1.7	1.6	4.1	2.5
Personal consumption expenditures	1.4	2.3	5.5	4.3	1.4	1.4	4.3	2.1
Goods	.4	2.1	8.2	5.7	.5	.7	6.3	2.2
Services	2.5	2.5	2.6	2.7	2.4	2.1	2.1	2.0
Gross private domestic investment	-26.0	7.0	9.6	7.5	4.1	3.1	3.7	4.9
Residential structures	-6.1	13.6	19.8	18.4	10.0	4.0	7.3	13.0
Business fixed investment	-4.7	-2.5	-.9	.8	1.9	2.2	2.2	2.1
Gov't. purchases of goods and services	-4.2	-2.5	.8	1.1	.9	1.3	1.9	2.3
Federal	-8.4	-3.9	4.5	4.1	3.8	5.0	5.2	6.1
National defense	2.6	4.5	4.5	9.2	7.8	7.6	8.5	8.8
State and local	-1.5	-1.5	-1.4	-.8	-.9	-1.0	-.3	-.2
Disposable personal income	-.8	.3	10.3	2.4	.3	.8	8.6	1.7
<u>Current dollars</u>								
Gross national product	2.5	8.2	10.9	10.0	7.0	6.5	8.7	8.1
Final purchases	6.0	7.4	10.0	9.6	6.9	6.4	8.7	8.1
Private	7.2	8.5	10.8	9.4	7.1	6.4	9.2	7.4
Excluding net exports	7.4	9.1	11.6	9.9	7.1	6.7	9.1	7.2
Personal consumption expenditures	8.8	9.4	12.0	9.6	6.6	6.4	9.2	6.6
Goods	6.2	8.0	13.6	10.7	5.0	4.8	10.1	6.1
Services	11.6	11.0	10.5	8.5	8.3	8.2	8.3	7.2
Gross private domestic investment	-20.1	13.8	15.8	13.8	9.7	8.2	8.7	10.1
Residential structures	.0	20.7	26.9	25.2	15.4	9.1	12.6	19.6
Business fixed investment	1.7	4.0	5.1	7.0	7.6	7.4	7.1	6.8
Gov't. purchases of goods and services	1.7	3.0	7.0	10.8	6.4	6.4	6.7	10.7
Federal	-4.2	-.7	9.5	19.0	8.9	9.5	9.7	19.7
National defense	6.2	10.1	9.9	25.7	13.5	13.0	13.3	23.0
State and local	5.7	5.5	5.5	5.6	4.7	4.3	4.7	4.7
Disposable personal income	6.4	7.4	17.1	7.6	5.4	5.8	13.7	6.2
Personal income	5.8	7.6	10.1	7.9	5.7	6.3	8.3	6.9
Wage and salary disbursements	3.3	6.1	7.8	9.7	6.5	6.7	7.6	8.6
Corporate profits with IVA & C.C. Adj.	-38.3	34.6	71.5	26.1	-1.2	.4	31.8	14.7
Corporate profits before tax	-39.7	21.0	49.4	14.9	-9.8	-9.0	17.4	2.8
Nonfarm payroll employment	-2.9	-.4	.5	1.5	.8	1.0	1.6	1.5
Manufacturing	-12.6	-2.3	1.7	5.4	2.6	2.5	3.3	3.9
Nonfarm business sector								
Output per hour	-.5	3.1	4.7	2.3	.6	.6	2.4	.9
Compensation per hour	8.5	7.8	7.8	7.4	7.5	6.6	6.5	6.3
Unit labor costs hour	9.0	4.6	3.0	5.0	6.9	6.0	4.0	5.4
GNP implicit deflator <u>1/</u>	6.7	6.9	6.1	6.1	5.5	5.0	4.7	5.3
Gross domestic business product								
fixed-weighted price index <u>2/</u>	6.9	7.3	6.8	5.9	5.5	5.3	5.1	5.0
Excluding food and energy	6.4	7.0	6.5	5.9	5.1	4.8	4.5	4.7
Consumer price index (all urban)	7.5	7.5	7.2	6.4	6.0	5.8	5.1	4.7
Industrial production	-13.0	4.9	8.4	4.7	3.0	2.7	5.5	4.8

1/ Excluding Federal pay increases, the rates of change are: 1982-Q1, 6.7 percent; 1982-Q4, 5.3 percent; 1983-Q1, 5.4 percent; 1983-Q4, 4.5 percent

2/ Uses expenditures in 1972 as weights.

CONFIDENTIAL - FR
CLASS II FOMC

GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Expenditures and income figures are billions of current dollars.)

	1976	1977	1978	1979	1980	1981	----Projected----	
							1982	1983
Gross national product	1718.0	1918.0	2156.1	2413.9	2626.1	2922.2	3107.2	3364.8
Final purchases	1706.2	1897.0	2133.9	2396.4	2632.0	2904.0	3106.9	3356.5
Private	1344.1	1502.5	1701.3	1922.6	2097.3	2314.4	2475.7	2678.8
Excluding net exports	1330.4	1506.7	1701.9	1909.2	2074.0	2290.6	2465.4	2673.7
Personal consumption expenditures	1084.3	1205.5	1348.7	1510.9	1672.8	1858.1	2024.1	2191.7
Goods	598.5	657.8	729.1	814.5	887.6	975.4	1040.2	1122.5
Services	485.7	547.7	619.6	696.3	785.2	882.7	983.9	1069.1
Gross private domestic investment	257.9	322.3	375.3	415.8	395.3	450.6	441.5	490.3
Residential construction	72.0	95.8	111.3	118.6	105.3	105.3	101.3	118.9
Business fixed investment	174.1	205.5	242.0	279.7	296.0	327.1	340.0	363.1
Change in business inventories	11.8	21.0	22.2	17.5	-5.9	18.2	.3	8.2
Nonfarm	13.9	20.2	21.8	13.4	-4.7	15.9	.3	8.2
Net exports of goods and services ^{1/}	13.7	-4.2	-.6	13.4	23.3	23.8	10.3	5.1
Exports	170.9	183.3	219.8	281.3	339.8	366.7	356.4	384.8
Imports	157.1	187.5	220.4	267.9	316.5	342.9	346.1	379.7
Gov't. purchases of goods and services	362.1	394.5	432.6	473.8	534.7	589.6	631.2	677.7
Federal ^{2/}	129.2	143.9	153.4	167.9	198.9	228.6	249.4	277.0
State and local	232.9	250.6	279.2	305.9	335.8	361.1	381.8	400.7
Gross national product in constant (1972) dollars	1300.4	1371.7	1436.9	1483.0	1480.7	1509.6	1495.7	1534.6
Personal income	1391.2	1538.0	1721.8	1943.8	2160.2	2403.6	2598.4	2787.1
Wage and salary disbursements	889.9	983.8	1105.2	1236.1	1343.7	1482.8	1576.4	1695.0
Disposable personal income	1194.4	1311.5	1462.9	1641.7	1821.7	2015.4	2201.1	2388.0
Saving rate (percent)	6.9	5.6	5.2	5.2	5.6	5.3	5.5	5.7
Corporate profits with I.V.A. and C.C. Adj.	138.1	164.7	185.5	196.8	182.7	189.0	170.8	201.5
Corporate profits before tax	166.3	192.6	223.3	255.4	245.5	230.3	194.9	207.7
Federal government surplus or deficit (N.I.A. basis)	-53.1	-46.4	-29.2	-14.8	-61.2	-61.6	-121.8	-149.6
High employment surplus or deficit (-)	-20.1	-23.0	-15.7	-2.2	-18.2	-.7	-17.5	-36.3
State and local government surplus or deficit (-) (N.I.A. basis)	16.6	28.1	29.0	26.7	29.1	36.5	37.0	42.6
Excluding social insurance funds	.9	10.1	9.0	2.9	2.1	4.4	.1	.5
Civilian labor force (millions)	94.8	97.4	100.4	102.9	104.7	106.5	107.5	108.6
Unemployment rate (percent)	7.7	7.0	6.0	5.8	7.1	7.6	9.4	9.2
Nonfarm payroll employment (millions)	79.4	82.5	86.7	89.8	90.6	91.6	90.9	91.8
Manufacturing	19.0	19.7	20.5	21.0	20.3	20.3	19.4	19.9
Industrial production (1967=100)	130.5	138.1	146.1	152.5	147.0	151.0	144.4	150.9
Capacity utilization: all manufacturing (percent)	79.5	81.9	84.4	85.6	79.1	78.4	72.4	73.7
Materials (percent)	81.1	82.7	85.6	87.4	80.0	80.0	72.3	74.7
Housing starts, private (million units, A.R.)	1.54	1.99	2.02	1.75	1.29	1.09	1.09	1.22
New auto sales, (millions, A.R.)	10.12	11.13	11.28	10.70	9.04	8.56	8.67	9.35
Domestic models	8.63	9.07	9.29	8.38	6.62	6.24	6.25	6.85
Foreign models	1.50	2.06	1.99	2.32	2.42	2.32	2.42	2.50

^{1/} Balance of payments data underlying these estimates are shown in the International Developments section of this part of the Greenbook.

^{2/} Components of purchases and total receipts and total expenditures are shown in the Federal Sector Accounts table which follows.

CONFIDENTIAL - FR
CLASS II FOMC

PERCENT CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1976	1977	1978	1979	1980	1981	--Projected--	
							1982	1983
<u>Constant (1972) dollars</u>								
Gross national product	5.4	5.5	4.8	3.2	-.2	1.9	-.9	2.6
Final purchases	4.2	5.2	4.7	3.5	.7	1.2	-.4	2.3
Private	5.3	6.0	15.4	4.0	.2	1.4	-.3	2.7
Excluding net exports	6.2	6.5	5.2	2.9	-1.0	2.1	.6	3.0
Personal consumption expenditures	5.6	4.9	4.7	2.9	.5	2.6	1.6	2.9
Goods	6.7	5.2	4.2	1.9	-1.4	2.5	.9	3.4
Services	4.3	4.5	5.4	4.1	2.6	2.6	2.4	2.4
Gross private domestic investment	-19.2	15.7	7.6	1.3	-12.5	5.6	-8.0	5.4
Residential structures	-21.3	18.5	2.9	-5.2	-18.6	-6.0	-8.9	11.5
Business fixed investment	-5.3	11.9	9.1	6.5	-3.0	2.0	-3.2	1.2
Gov't. purchases of goods and services	.0	2.1	2.0	1.5	2.9	.4	-.6	1.0
Federal	-.7	4.1	-.9	1.9	6.3	2.7	1.0	4.0
National defense	-2.3	.8	.0	2.6	5.7	3.7	5.2	9.9
State and local	.5	.9	3.7	1.2	1.0	-.9	-1.6	-.9
Disposable personal income	3.6	3.6	4.4	3.1	.7	2.1	1.9	3.1
<u>Current dollars</u>								
Gross national product	10.9	11.6	12.4	12.0	8.8	11.3	6.3	8.3
Final purchases	9.6	11.2	12.5	12.3	9.8	10.3	7.0	8.0
Private	10.5	11.8	13.2	13.0	9.1	10.4	7.0	8.2
Excluding net exports	11.8	13.3	12.9	12.2	8.6	10.4	7.6	8.4
Personal consumption expenditures	11.1	11.2	11.9	12.0	10.7	11.1	8.9	8.3
Goods	10.9	9.9	10.8	11.7	9.0	9.9	6.6	7.9
Services	11.2	12.7	13.1	12.4	12.8	12.4	11.5	8.7
Gross private domestic investment	25.1	25.0	16.5	10.8	-4.9	14.0	-2.0	11.0
Residential structures	30.2	33.1	16.1	6.6	-11.3	.1	-3.8	17.4
Business fixed investment	10.3	18.1	17.7	15.6	5.8	10.5	4.0	6.8
Gov't. purchases of goods and services	6.5	8.9	9.7	9.5	12.9	10.3	7.1	7.4
Federal	5.3	11.4	6.6	9.5	18.5	14.9	9.1	11.1
National defense	3.7	8.5	7.1	11.2	18.4	16.4	14.8	15.5
State and local	7.3	7.6	11.4	9.6	9.8	7.5	5.7	4.9
Disposable personal income	9.0	9.8	11.5	12.2	11.0	10.6	9.2	8.5
Personal income	10.0	10.6	12.0	12.9	11.1	11.3	8.1	7.3
Wage and salary disbursements	10.4	10.6	12.3	11.8	8.7	10.4	6.3	7.5
Corporate profits with IVA & C.C. Adj.	25.0	19.3	12.6	6.1	-7.2	3.4	-9.6	18.0
Corporate profits before tax	25.9	15.8	15.9	14.4	-3.9	-6.2	-15.4	6.6
Nonfarm payroll employment	3.2	3.9	5.1	3.6	.8	1.0	-.2	.2
Manufacturing	3.7	3.6	4.2	2.6	-3.5	.0	-.2	.1
Nonfarm business sector								
Output per hour	3.2	2.0	-.2	-.7	-.3	.9	-.2	1.8
Compensation per hour	8.1	7.6	8.5	9.7	9.9	10.0	8.4	7.2
Unit labor costs	4.7	5.5	8.7	10.4	10.3	9.0	8.2	5.3
GNP implicit deflator	5.2	5.8	7.3	8.5	9.0	9.1	7.3	5.6
Gross domestic business product								
fixed-weighted price index ^{1/}	5.5	6.3	7.8	9.7	9.8	9.4	7.4	5.7
Excluding food and energy	6.0	6.5	7.5	8.4	8.2	9.0	7.6	5.4
Consumer price index (all urban)	5.8	6.5	7.7	11.3	13.5	10.3	8.0	6.1
Industrial production	10.8	5.8	5.8	4.4	-3.5	2.7	-4.3	4.5

^{1/} Uses expenditures in 1972 weights.

FEDERAL SECTOR ACCOUNTS
(billions of dollars)

	Fiscal Year* 1981	FRB Staff Estimates														
		FY1982e/		FY1983e/		CY1982e/		Calendar quarters; unadjusted data								
		Admn. 1/	F.R. Board	F.R. Board	CY 1981e/	F.R. Board	1981			1982			1983			
							III*	IV	I	II	III	IV	I	II	III	
Unified budget receipts	602.6	662.4	626.8	635.2	622.1	619.0	156.7	146.5	143.8	186.8	149.6	138.8	149.7	191.5	155.3	
Unified budget outlays	660.5	704.8	733.6	777.3	692.3	735.0	165.3	192.3	166.7	185.5	189.0	193.8	195.4	194.6	193.5	
Surplus/deficit(-), unified budget	-57.9	-42.5	-106.8	-142.0	-70.2	-116.0	-8.6	-45.8	-22.9	1.3	-39.4	-55.0	-45.7	-3.1	-38.2	
Surplus/deficit(-), off-budget agencies ²	-21.0	-18.2	-20.5	-18.4	-23.4	-19.9	-6.9	-4.5	-5.9	-4.8	-5.3	-3.9	-5.0	-4.7	-4.9	
Combined deficit to be financed	-78.9	-60.7	-127.3	-160.4	-93.5	-135.9	-15.5	-50.3	-28.8	-3.5	-44.7	-58.8	-50.8	-7.8	-43.1	
Means of financing combined deficit:																
Net borrowing from public	79.4	59.0	121.7	161.7	87.4	142.7	18.5	35.7	34.3	9.4	42.3	56.7	48.5	18.2	38.3	
Decrease in cash operating balance	2.3	0.0	2.7	0.9	0.3	1.2	-2.3	6.7	1.5	-5.1	-0.4	5.2	-1.3	-6.6	3.6	
Other ³	-2.8	1.7	2.9	-2.1	5.8	-8.1	-0.7	8.0	-7.0	-0.9	2.8	-3.0	3.5	-3.8	1.2	
Cash operating balance, end of period	18.7	18.7	16.0	15.1	12.0	10.8	18.7	12.0	10.5	15.6	16.0	10.8	12.1	18.7	15.1	
Memo: Sponsored agencies borrowing ⁴	37.7	n.a.	17.8	24.0	31.0	21.7	15.4	2.9	3.1	6.5	5.3	6.8	4.0	6.6	6.6	
NIA Budget																
							Seasonally adjusted annual rates									
Receipts	612.5	678.3	626.3	644.7	624.9	629.2	638.3	622.9	624.3	637.0	620.8	634.6	648.2	656.3	639.5	
Expenditures	666.8	719.3	737.3	787.0	686.4	751.0	694.0	719.4	727.6	737.9	764.4	774.0	779.9	787.3	806.7	
Purchases	219.9	247.4	246.0	269.3	228.6	249.4	226.4	246.7	244.1	243.7	249.3	260.4	266.0	272.1	278.5	
Defense	147.3	171.7	170.8	196.0	153.3	176.0	154.1	165.8	168.3	172.4	176.5	186.9	192.9	198.9	205.2	
Nondefense	72.6	75.7	75.2	73.3	75.2	73.4	72.2	81.0	75.8	71.3	72.8	73.5	73.1	73.2	73.3	
All other expenditures	446.9	471.9	491.3	517.7	457.8	501.6	467.6	472.7	483.5	494.2	515.1	513.6	513.9	515.2	528.2	
Surplus/deficit(-)	-54.3	-41.0	-111.1	-142.3	-61.5	-121.8	-55.7	-96.4	-103.3	-100.9	-143.6	-139.4	-131.7	-131.0	-167.2	
High-Employment (H.E.) surplus/deficit(-) evaluated at H.E. unemployment rate of:																
5.1 percent	1.3	n.a.	-14.6	-30.7	-0.7	-17.5	11.5	-21.1	-7.0	7.0	-37.4	-32.5	-20.2	-14.7	-55.4	
6.1 percent	-25.3	n.a.	-41.6	-58.9	-27.7	-44.9	-19.2	-47.2	-33.9	-20.8	-64.6	-60.2	-48.5	-43.5	-83.4	
		*--actual		e--estimated				n.a.--not available								

1. OMB Mid-Session Review of the 1982 Budget, July 1981. On September 24, 1981, the Administration presented revised estimates of unified budget receipts and outlays for FY1982. The Fall Budget Program Fact Sheet estimates receipts of \$666.2 billion and outlays of \$709.3 billion for a deficit of \$43.1 billion.

2. Includes Federal Financing Bank, Postal Service Fund, Rural Electrification and Telephone Revolving Fund, and Rural Telephone Bank, and SPR in FY1982 only.

3. Checks issued less checks paid, accrued items and other transactions.

4. FRB staff estimates include Federal Home Loan Banks, FNMA, Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives marketable debt on an offering basis.

NOTE: Quarterly figures may not add to yearly totals due to rounding.

DOMESTIC FINANCIAL DEVELOPMENTS

Summary. Market interest rates have backed up further since the last FOMC meeting. The surge in narrow money growth that began in November continued through the first half of January, and reserve positions of depository institutions tightened. A substantial rise in the level of adjustment borrowings was associated with an upward movement in the federal funds rate of 1-1/2 percentage points, and other short-term rates also rose 1 to 2 percentage points.

Treasury and corporate bond yields have registered increases of about 1/2 percentage point since the last Committee meeting, against a backdrop of rising short-term rates, as well as deepening pessimism regarding the prospective conflict between record government deficits and monetary restraint. Municipal bond rates have risen by less on balance, but briefly touched new record levels in the interim; the ratio of tax-exempt to taxable bond yields remains near the historic high of mid-December, in part because property and liability insurance companies have continued to eschew tax-exempt securities in light of record underwriting losses last year. Commitment rates on conventional fixed-rate mortgages in primary markets have increased by about 3/4 percentage point since the last FOMC meeting and the ceiling rate on FHA/VA home mortgages was hiked one full percentage point.

The growth of M1 in December slowed only a little from the rapid month-earlier pace, and a marked acceleration in growth of this aggregate is assured for January. Some of the surge in M1 demand since October may have been in response to the substantial drop in interest rates that occurred late last summer and early in the fall. Over the last

three months the growth of other checkable deposits has been very large. This development, which occurred along with an upturn in savings deposits, may reflect a strengthened liquidity preference in the face of heightened economic uncertainty.

M2 growth decelerated in December from the month-earlier pace, but still remained at a relatively strong 11-1/4 percent. Data through mid-January point to an expansion of M2 around its December rate of growth. Small time deposits showed little gain over the two months and inflows to money market mutual fund shares were reduced as relative yields switched in mid-December to favor open market alternatives to MMMFs. On the other hand, inflows to savings deposits and overnight RPs and Eurodollars were sizable.

The growth of M3 probably continued in double digits in January; early in the month thrift institutions continued to issue large time deposits in volume, and commercial banks again raised funds through large CDs to help finance apparently robust loan demand. Business loan growth at large banks was particularly strong in the first half of January, on the heels of a tremendous surge at these banks in December. Commercial and industrial loans at all commercial banks grew at over a 20 percent annual rate in December, abstracting from shifts of loans booked at domestic banking offices to International Banking Facilities.

The stepped-up business borrowing at domestic banks in December and January reflected a change in the composition of sources of credit in an environment of reduced overall credit flows to nonfinancial firms. Bond issuers quickly pulled back from domestic markets as corporate bond yields rose from their late November troughs, although several companies have

offered zero coupon, deep discount bonds abroad with considerable success. Borrowing by U.S. residents from foreign branches of U.S. banks also has slackened, returning to U.S. offices, as a reduced spread between the prime and Eurodollar rates has lessened the attractiveness of LIBOR pricing options. Finally, with a narrowing of the spread between commercial paper and bank lending rates, issuance of nonfinancial commercial paper appears to have dried up in January, following a sizable increase in the previous month.

Growth in consumer installment credit dropped to a 1 percent annual rate during November--the slowest pace since the end of the credit restraint program in July 1980. The volume of mortgage takedowns toward year-end apparently remained quite depressed. Mortgage holdings at S&Ls actually declined in November for the second month in a row, although a strengthening of net mortgage lending appeared at federal agencies and commercial banks in December.

Outlook. Short-term interest rates appear likely to remain around their recent higher levels in the near term, as the System constrains reserve availability in order to slow the growth of money. However, as the recent surge in M1 unwinds, some easing of money market conditions may occur if the economy is as slow in gathering upward momentum as the staff projects.

The bond markets may have to contend with uncertainties about the federal budgetary outlook for a time, but at least a small rally would seem likely with any moderation of short-term rates. If a further perceptible slowing of wage and price inflation occurs, the bond markets could experience a more forceful rally. Any noticeable improvement should

produce a moderation of the recent pace of C&I lending at commercial banks as firms fund their shorter-term debt in capital markets. In any event, the overall financing gap of the nonfinancial corporate sector is not expected to change appreciably in coming months.

Government borrowing will remain substantial. Federal marketable borrowing is projected at about \$36 billion (NSA) in the first quarter and at a relatively high level even during the spring when tax receipts typically permit a net paydown. By contrast, reflecting the recent falloff of issuance of mortgage revenue bonds, total state and local long-term offerings in coming months are likely to remain below the pace of the fourth quarter.

As other rates ease, mortgage rates should resume a downward course, and mortgage lending is likely to pick up a little from the depressed fourth quarter pace. Thrift institutions, though, are expected to continue to place a large share of their assets in more liquid forms. Growth in consumer installment credit is projected to be moderate.

INTERNATIONAL DEVELOPMENTS

Summary. The weighted average value of the dollar has moved up about 1-1/2 percent since the last FOMC meeting -- mostly in the last ten days. Gains were somewhat greater than average against the Japanese yen and the French and Belgian franc, and less against the German mark and the Canadian dollar. Current interest rate developments, and changing expectations about future rates, were the major influence on the market. While interest rates on short-term dollar assets have firmed, representative foreign rates have dropped noticeably in recent weeks as authorities in several countries have moved to reduce their rates: in Germany the Bundesbank has lowered its special Lombard rate by 1/2 percentage point; the Netherlands Bank lowered its official rates by 1/2 percentage point; the Bank of England has gradually lowered its offering rates on short-term bills by 1/2 percentage point; and Japan has been cautiously easing credit conditions since December.

Evidence about the rate of economic activity abroad is somewhat mixed for the fourth quarter, though the readiness of several countries to ease monetary policy and accept depreciating currencies reflects concern about feeble economic growth and rising unemployment. Rates of inflation generally remain high abroad, with the exception of Japan, but some improvement may be emerging in Germany and the United Kingdom.

Weakness in domestic activity has helped improve the external balance of several countries -- especially Germany, Japan, and Italy.

For the United States, however, continued weak demand abroad and the high value of the dollar produced much larger trade deficits in October/November -- annual rates of close to \$50 billion, twice the rate of the first nine months of the year. Export volume is down, though the drop has shown up mainly in a few sectors -- aircraft, autos to Canada, and gold. Meanwhile, import volume in October/November was higher across a broad range of commodities, despite the lower level of U.S. economic activity.

In the U.S. capital accounts there were sizable outflows of private capital in November, as U.S. interest rates eased relative to those abroad. This showed up as a large net outflow through banking channels and also as a jump to a \$2 billion net outflow for the month in securities transactions as foreign borrowers took the opportunity to tap the U.S. bond market. The net banking outflow appears to have been largely reversed in December, and new issues also tapered off. Credit extended to U.S. borrowers by foreign branches of U.S. banks rose about \$3 billion between September and November, to about \$12 billion, and has risen only slightly since then.

In international capital markets more generally, the volume of newly announced medium-term Eurocredits, and of bonds sold internationally, rose substantially in 1981. The total of Eurocredits announced jumped \$55 to \$132 billion, including a \$47 billion increase for U.S.

borrowers (mainly related to take-overs and including sizable amounts not drawn down), and a \$9 billion increase in loans arranged for non-OPEC developing countries -- from a relatively low 1980 base. Credits announced for Communist countries dropped to negligible amounts by mid-year. Sales of bonds in international markets also rose substantially in 1981 -- by \$11 billion to a total of \$54 billion. A considerable part of the increase represented sales in the U.S. market, as noted above.

Outlook. Economic recovery in major foreign countries is expected to be gradual this year (GNP growth of about 2 percent Q4-Q4), accompanied by declining inflation rates and somewhat greater unemployment. The combined current-account deficit of these countries is likely to drop sharply in 1982, with Japan posting a rising surplus, and Germany moving from deficit to surplus. Beyond 1982, the pace of economic activity abroad is projected to rise to about 3 percent annually, with price inflation falling further, and current accounts tending to stabilize.

The U.S. current account is projected to show a deficit in 1982 of about \$10 billion -- moderately higher than projected a month ago -- and a larger deficit in 1983. The higher deficits reflect a number of factors, including some reassessment of the outlook for merchandise trade in the light of the exceptionally large deficits in October/November. Also, the average exchange rate of the dollar is currently above the level expected a month ago, and is projected to decline gradually over the period ahead as the U.S. current account deficits develop.

OUTLOOK FOR U.S. NET EXPORTS AND RELATED ITEMS
(BILLIONS OF DOLLARS, SEASONALLY ADJUSTED ANNUAL RATES)

January 27, 1982

	1981 ANN.	1982 ANN. ^p	1983 ANN. ^s	1982 Q I ^s	1982 Q II ^s	1982 Q III ^s	1982 Q IV ^s	1983 Q I ^s	1983 Q II ^s	1983 Q III ^s	1983 Q IV ^s
1. GNP NET EXPORTS											
CURRENT \$, NET	23.8	10.8	5.1	15.3	12.4	8.2	5.4	5.5	3.9	4.9	6.3
EXPORTS OF G&S	366.7	356.4	384.8	354.1	352.3	355.8	363.4	371.7	378.8	389.3	399.5
IMPORTS OF G&S	342.9	346.1	379.7	338.8	339.9	347.7	358.0	366.3	374.9	384.5	393.2
CONSTANT 72 \$, NET	44.2	33.7	31.0	36.5	34.3	32.6	31.5	30.9	30.3	31.0	31.9
EXPORTS OF G&S	160.0	148.1	149.2	150.2	147.4	146.9	147.8	147.8	148.1	149.7	151.1
IMPORTS OF G&S	115.8	114.4	118.1	113.7	113.2	114.3	116.3	116.9	117.8	118.7	119.2
TERMS OF TRADE (1972=100) 1/	77.3	79.5	80.3	79.1	79.5	79.6	79.8	80.3	80.4	80.3	80.2
2. U.S. MERCHANDISE TRADE BALANCE 2/											
	-28.9 ^p	-38.0	-45.1	-34.7	-33.4	-39.0	-44.9	-45.7	-45.3	-45.3	-44.2
EXPORTS (EXCL. MILITARY)	237.6 ^p	229.5	246.2	231.1	229.1	228.7	230.5	236.2	241.8	249.2	257.6
AGRICULTURAL	44.6 ^p	46.7	51.8	45.9	46.0	46.8	48.2	50.0	51.2	52.4	53.8
NONAGRICULTURAL	193.0 ^p	183.2	194.4	185.3	183.1	181.9	182.3	186.2	190.6	196.8	203.8
IMPORTS	266.5 ^p	267.5	291.3	265.8	262.5	267.7	275.4	282.0	287.1	294.4	301.8
PETROLEUM AND PRODUCTS	78.6 ^p	68.2	70.4	68.1	68.1	68.1	68.4	68.8	69.1	71.0	72.7
NONPETROLEUM	188.0 ^p	199.7	220.9	197.6	194.4	199.6	207.0	213.1	217.9	223.4	229.1
3. U.S. CURRENT ACCOUNT BALANCE											
	4.3 ^p	-11.8	-19.3	-6.1	-8.8	-14.0	-18.4	-18.8	-19.8	-19.8	-19.0
OF WHICH: NET INVESTMENT INCOME	36.6 ^p	32.6	33.0	34.4	31.1	31.5	33.3	33.9	32.3	32.6	33.0
4. FOREIGN OUTLOOK - TEN INDUSTRIAL COUNTRIES 3/											
REAL GNP, % CHANGE, ANNUAL RATES	.4 ^p	1.5	2.6	1.5	1.7	2.1	2.4	2.7	2.7	2.9	3.1
CONSUMER PRICES, 4/, % CHANGE, ANNUAL RATES	9.7 ^p	8.9	7.6	9.2	9.1	8.1	7.6	7.7	7.4	7.0	6.8

1/ GNP EXPORT IMPLICIT DEFLATOR DIVIDED BY GNP IMPORT IMPLICIT DEFLATOR.

2/ INTERNATIONAL ACCOUNTS BASIS.

3/ GEOMETRIC WEIGHTS USED TO AGGREGATE FOREIGN REAL GNP AND CONSUMER PRICES -- PERCENT SHARE IN TEN-COUNTRY TOTAL MULTILATERAL TRADE. CANADA (9.1%), JAPAN (13.6%), UNITED KINGDOM (11.9%), GERMANY (20.8%), FRANCE (13.1%), ITALY (9.0%), BELGIUM (6.4%), THE NETHERLANDS (8.3%), SWITZERLAND (3.6%), SWEDEN (4.2%).

p/ PROJECTED.